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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1941

No. 1033

**DAKOTA TRACTOR AND EQUIPMENT COMPANY,
A CORPORATION,**

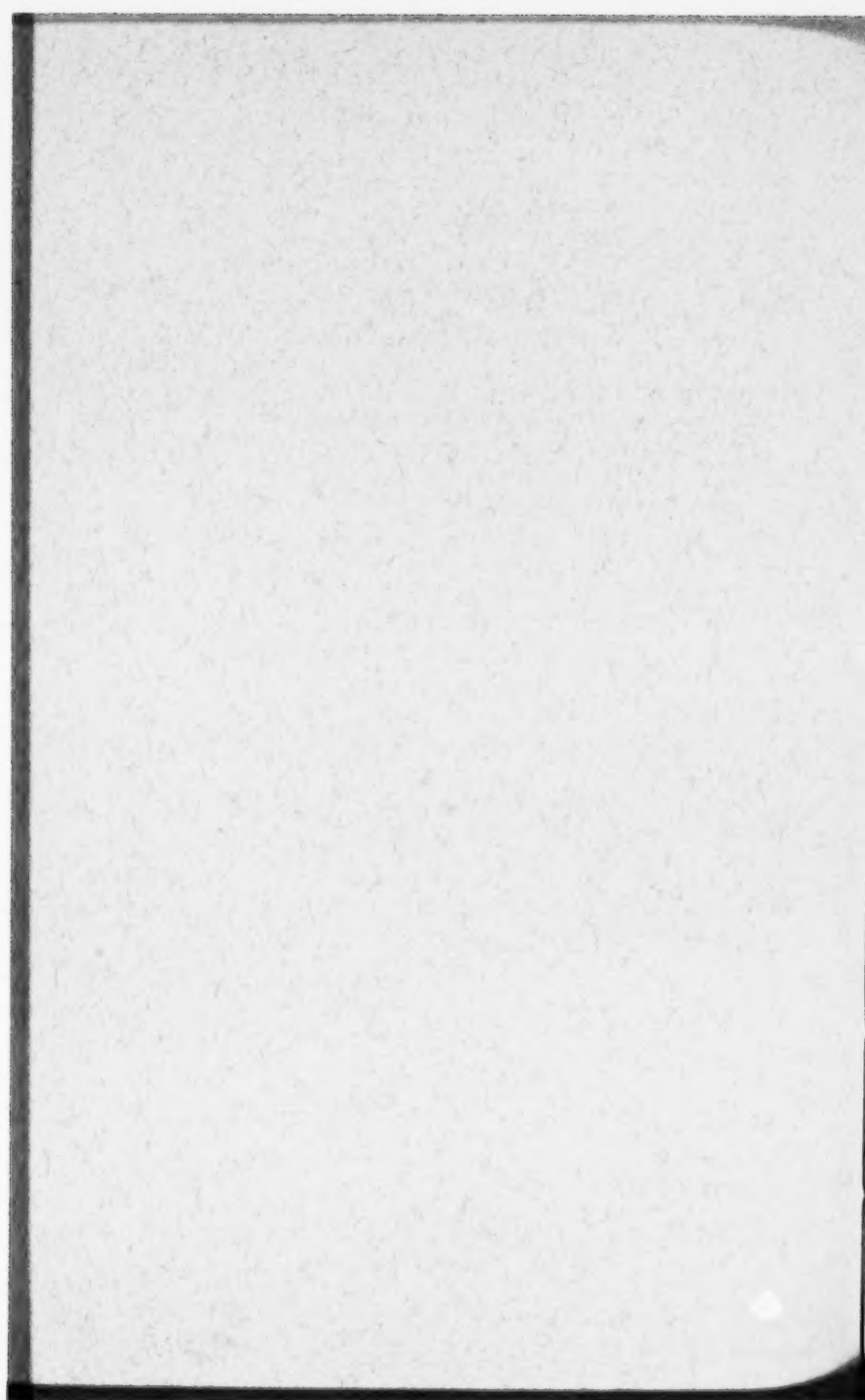
Petitioner,

vs.

THE UNITED STATES OF AMERICA.

**PETITION FOR WRIT OF CERTIORARI TO THE
UNITED STATES CIRCUIT COURT OF APPEALS
FOR THE EIGHTH CIRCUIT.**

**W. H. SHURE,
E. T. CONMY,**
Counsel for Petitioner.



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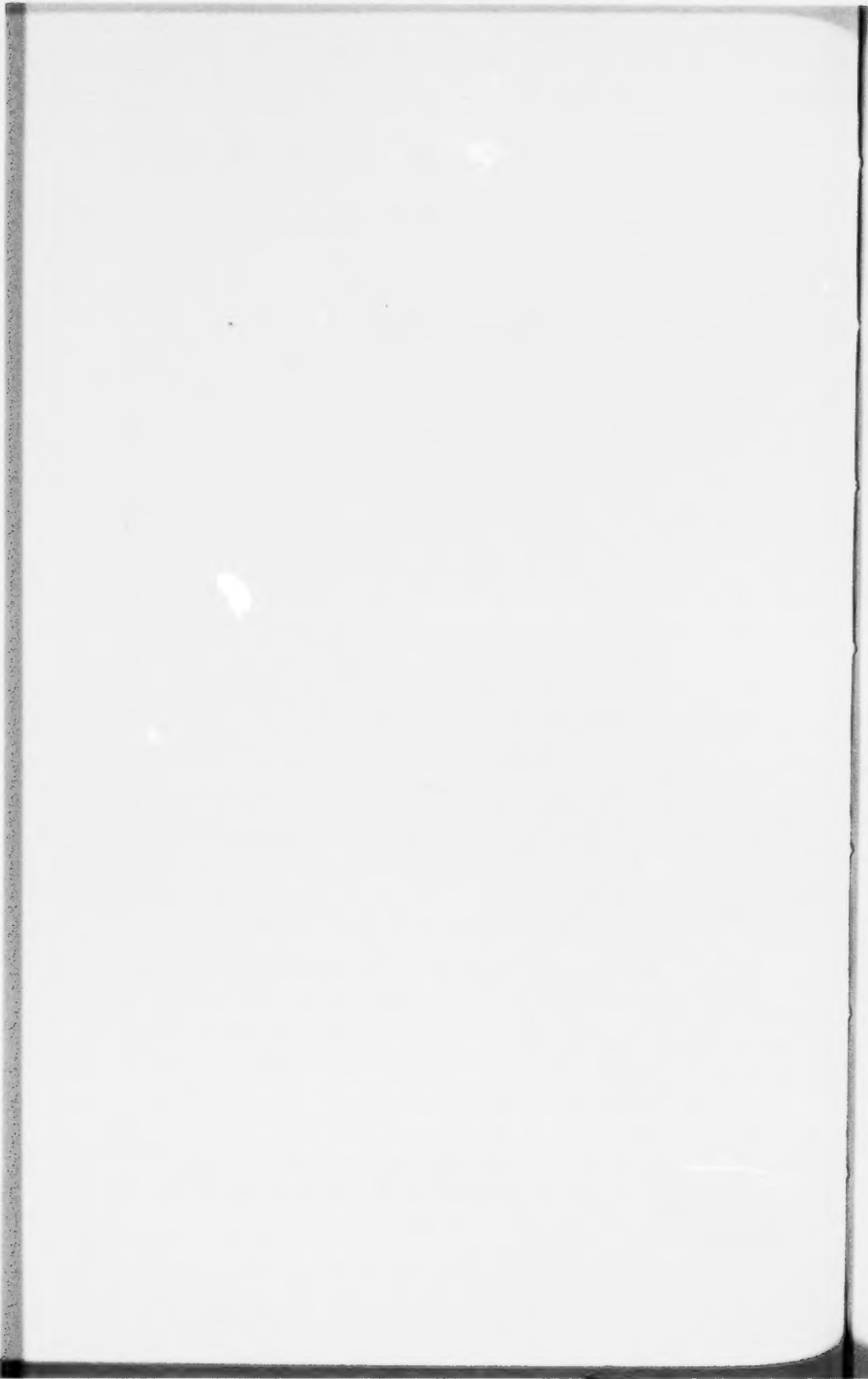
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DAKOTA TRACTOR AND EQUIPMENT COMPANY,
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vs.

Petitioner,

THE UNITED STATES OF AMERICA.

PETITION FOR WRIT OF CERTIORARI.

*To the Honorable the Chief Justice of the United States and
Associate Justices of the Supreme Court of the United
States:*

Summary Statement of Matter Involved.

In the petitioner and taxpayer's 1936 income tax return it claimed a credit in the computation of the surtax on undistributed profits under Section 26 (c) (1) of the Revenue Act of 1936 (R. 9, 27-37, 89). This credit was disallowed, a deficiency in amount \$5,832.19 was assessed accordingly and paid, claim for refund was filed for the amount paid and rejected and this suit was brought for the recovery of that amount (R. 9-10, 39-49, 50-53, 55-58, 59, 89-90).

The credit was claimed under Section 26 (c) of the 1936 Revenue Act (R. 9, 27, 89) which reads as follows:

SEC. 26. CREDITS OF CORPORATIONS.

In the case of a corporation the following credits shall be allowed to the extent provided in the various sections imposing tax—

* * * * *

(c) Contracts Restricting Payment of Dividends—

(1) Prohibition on Payment of Dividends—An amount equal to the excess of the adjusted net income over the aggregate of the amounts which can be distributed within the taxable year as dividends without violating a provision of a written contract executed by the corporation prior to May 1, 1936, which provision expressly deals with the payment of dividends. If a corporation would be entitled to a credit under this paragraph because of a contract provision and also to one or more credits because of other contract provisions, only the largest of such credits shall be allowed, and for such purpose if two or more credits are equal in amount only one shall be taken into account.

* * * * *

The contract under which the credit was claimed is printed in full at pages 82, 83, and 84 of the record and in brief it provides that "There shall be no cash withdrawals from the business in the form of cash dividends or otherwise until entire authorized capital stock of \$100,000.00 has been paid in". It also provides that "all profits shall remain in the business and from time to time the earned surplus shall be converted into paid-in capital through the declaration of stock dividends or otherwise."

The trial court held that the contract letter of May 13th, 1935, came within Section 26 (c) (1) and gave judgment to

petitioner (R. 90-91). This judgment was set aside by the Circuit Court, it holding that the word "dividends" meant dividends of all kinds and said "Since this contract letter prohibited payment only of dividends in the form of cash or property, it falls short of the requirements of 26 (c) (1) and can be no basis for the credit allowed thereby" (R. 111).

Reasons Relied On for Allowance of Writ.

The allowance of a Writ of Certiorari is respectfully asked for the following reasons:

1st. The Circuit Court in reversing the trial court here has decided an important question of Federal law which has not been, but should be, settled by this court. The record here shows there are two litigants who are so vitally interested in this question that they tried to intervene here (R. 122). That Section 26 (c) (1) is the subject of a steadily increasing volume of litigation is clear (see C. C. H. 1942 Federal Tax Service, Volume 1, Paragraph 367.20 et al., and Index Volume, "Cumulative Numerical Index", Paragraph 367), and it is reasonable to suppose that the issue here involved is present in numerous cases not yet in the appellate courts.

2nd. The Circuit Court has rendered a decision in conflict with a decision of the Board of Tax Appeals. See *Paraport Theatre Leasing Corporation v. Commissioner*, 44 B. T. A. 108, where the word "dividends" was held to mean *taxable dividends*.

The vital and controlling point for decision is the meaning of the word "dividends" as used in Section 26 (c) (1). We submit that the Circuit Court has overlooked and not given consideration to Section 115 (A) or to Section 115 (F) (1) of the 1936 Act.

Section 115 (A) reads as follows:

“(a) Definition of Dividend. The term ‘dividend’ when used in this title (except in section 203 (a) (3) and section 207 (c) (1), relating to insurance companies) means any distribution made by a corporation to its shareholders, whether in money or in other property, (1) out of its earnings or profits accumulated after February 28, 1913, or (2) out of the earnings or profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distributions made during the taxable year), without regard to the amount of the earnings and profits at the time the distribution was made.”

No money was distributed and as a stock dividend does not distribute property, no property was distributed.

See: *Eisner v. Macomber*, 252 U. S. 211;

Williams v. Tel. Co., 93 N. Y. 189.

So we have the Act itself defining dividends and surely such a definition is controlling. Our contract prohibited dividends as defined by the Act so should entitle us to a credit.

Inasmuch as stock dividends sometimes do constitute a distribution of property we find the congress including in the Act in question Section 115 (F) (1) which reads as follows:

“General rule. A distribution made by a corporation to its shareholders in its stock or in rights to acquire its stock shall not be treated as a dividend to the extent that it does not constitute income to the shareholder within the meaning of the Sixteenth Amendment to the Constitution.”

This section makes more clear, we submit, that stock dividends which do not distribute property, such as were made here, are not “dividends” under Section 26 (c) (1).

In our view the word "dividends" in Section 26 (c) (1) should be construed as embracing only such distributions as diminish the corporation's assets. This is its commonly-accepted meaning and natural import in the business world (cf. *Lynch v. Hornby*, 247 U. S. 339, 346), and under familiar rules of construction (*Woolford Realty Co. v. Rose*, 286 U. S. 319, 327) is the meaning that should be attributed to it as used in the statute. Moreover, the intent of the statute was the prevention of the avoidance of surtax by accumulation of income, which a stock dividend does not do, and it is the intent, we are admonished (*Helvering v. Stockholms &c. Bank*, 293 U. S. 84, 93), that is controlling. Furthermore, contracts restricting payment of dividends customarily are for the benefit of creditors to prevent diminution of security, and it is only asset-distributions that make for such diminution. By the same token it is only asset-distributions that commonly are prohibited, with the result that if the Circuit Court's interpretation be adopted, the statute is robbed of a great deal of utility and is reduced to a practical nullity—something that should never be allowed. *Carbon Steel Co. v. Lewellyn*, 251 U. S. 501, 504, 505, 506.

Your petitioner believes that the judgment of the Circuit Court of Appeals is erroneous, and that this honorable court should require the said case to be certified to it for its review and determination, in conformity with the provisions of the Act of Congress in such cases made and provided.

WHEREFORE, your petitioner respectfully prays that a writ of certiorari may be issued out of and under the seal of this Court, directed to the United States Circuit Court of Appeals for the Eighth Circuit, commanding the said court to certify and send to this Court, on a day certain to be therein designated, a full and complete transcript

of the record and all proceedings of the said Circuit Court of Appeals in the said case therein, entitled United States of America, Appellant, v. Dakota Tractor & Equipment Company, A Corporation, Appellee, No. 12,014 at Law, to the end that the said case may be reviewed and determined by this Court as provided in Judicial Code, Sec. 240, or that your petitioner may have such other or further relief or remedy in the premises as to this Court may seem appropriate and in conformity with the said Act, and that the said judgment of the said Circuit Court of Appeals in the said case, and every part thereof, may be reversed by this Honorable Court.

And your petitioner will ever pray.

W. H. SHURE,
E. T. CONMY,
Attorneys for Petitioner.



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In the Supreme Court of the United States

OCTOBER TERM, 1941

No. 1033

DAKOTA TRACTOR & EQUIPMENT COMPANY, A CORPORATION, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINIONS BELOW

The District Court rendered no opinion. The opinion of the Circuit Court of Appeals (R. 98-108) is reported in 125 F. (2d) 20.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on January 7, 1942 (R. 108-109). A petition for rehearing was denied February 3, 1942 (R. 117). The petition for a writ of certiorari was filed March 11, 1942. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether a written contract prohibiting taxpayer from making cash dividend payments only, but allowing other dividend payments, entitled it to the credit allowed by Section 26 (c) (1) of the Revenue Act of 1936 in the computation of surtax on undistributed profits imposed by Section 14 of that Act.

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1936, c. 690, 49 Stat. 1648:

SEC. 26. CREDITS OF CORPORATIONS.

In the case of a corporation the following credits shall be allowed to the extent provided in the various sections imposing tax—

* * * *

(c) *Contracts restricting payment of dividends.*—

(1) *Prohibition on payment of dividends.*—An amount equal to the excess of the adjusted net income over the aggregate of the amounts which can be distributed within the taxable year as dividends without violating a provision of a written contract executed by the corporation prior to May 1, 1936, which provision expressly deals with the payment of dividends. * * *

Treasury Regulations 94, promulgated under the Revenue Act of 1936:

ART. 26-2. *Credit in connection with contracts restricting payment of dividends.*—

(a) The credit provided in section 26 (c) with respect to contracts restricting the payment of dividends is not available under every contract which might operate to restrict the payment of dividends, but only with respect to those provisions of written contracts executed by the corporation prior to May 1, 1936, which satisfy the conditions prescribed in the Act. * * *

* * * * *

(b) *Prohibition on payment of dividends.*—The credit provided in section 26 (c) (1) is allowable only with respect to a written contract executed by the corporation prior to May 1, 1936, which expressly deals with the payment of dividends and operates as a legal restriction upon the corporation as to the amounts which it can distribute within the taxable year as dividends. If an amount can be distributed within the taxable year as a dividend—

(1) in one form (as, for example, in stock or bonds of the corporation) without violating the provisions of a contract, but cannot be distributed within the taxable year as a dividend in another form (as, for example, in cash) without violating such provisions, * * *

* * * * *

then the amount is one which, under section 26 (c) (1), can be distributed within the taxable year as a dividend without violating such provisions.

STATEMENT

The facts as found by the District Court (R. 85-90) may be summarized as follows:

On May 27, 1935, petitioner and the Caterpillar Tractor Company executed a "Distributor's Sales and Service Agreement" under which petitioner was granted the right to act as distributor for the products of Caterpillar in a designated territory (R. 11-26, 86). This agreement did not include any provision dealing with the payment of dividends (R. 11-26), and was expressly stated to be the entire contract of the parties (R. 25). The District Court, however, admitted in evidence a letter dated May 13, 1935, which stated certain "policies" that the petitioner would carry out in the event that a distributor's agreement should be signed, and which the District Court found that Caterpillar had required before it would execute the distributor's agreement (R. 62, 81, 82-84, 90). Among the "policies" stated in that letter were the following (R. 82, 83-84):

3. The authorized capital stock of the company will be increased from \$50,000.00 to \$100,000.00 as promptly as possible.

* * * * *

5. Through the declaration of stock dividends or other satisfactory means the present surplus will be converted to paid-in capital stock of the company so that the outstanding capital stock will be increased to \$65,000.00.

* * * * *

All profits shall remain in the business and from time to time the earned surplus will be converted into paid-in capital through the declaration of stock dividends or otherwise.

As there is no desire to adversely affect the financial position of the company there shall be no cash withdrawals from the business in the form of cash dividends or otherwise until entire authorized capital stock of \$100,000.00 has been paid in.

As it is the desire of the company to become financially self-sustaining, and to operate the business in a manner that will meet the requirements of all of the manufacturers represented, particularly Caterpillar Tractor Co., the approval of Caterpillar Tractor Co. will be obtained before any cash is withdrawn from the business, even after the authorized capital of \$100,000.00 is paid in, unless at such time the business is actually fully self-sufficient financially and does not owe any money to Caterpillar Tractor Co.

If the volume of the business engendered shall justify increase of the net worth of the business above \$100,000.00, as it is expected will be the case, the authorized capital stock shall later be increased from time to time as may seem to be advisable and further earnings or additional cash be invested in the business and capital stock issued therefor until such time as the business becomes fully self-sufficient financially.

On January 1, 1936, the authorized capital stock of petitioner was \$100,000, consisting of 1,000 shares of common stock of \$100 par value, of which 325 shares were issued and outstanding. As a result of stock dividends authorized and issued during 1936, and a small aggregate of sales of common stock, \$100,000 of the petitioner's authorized capital stock was issued and outstanding on December 31, 1936 (R. 86).

The District Court concluded that the distributor's agreement and letter constituted a contract under which a credit was allowable to the petitioner in computing its surtax on undistributed profits (R. 90-91), and entered judgment for refund to the petitioner (R. 91). The Circuit Court of Appeals reversed (R. 108-109). A petition for rehearing was filed by the petitioner on January 28, 1942 (R. 111-116), and was denied by the Circuit Court of Appeals on February 3, 1942 (R. 117).

ARGUMENT

The decision of the court below is correct and no further review is warranted.

The agreement between petitioner and the Caterpillar Tractor Company, viewed in a light most favorable to petitioner, restricts the payment only of cash dividends (R. 106). Under the agreement, payment of stock dividends was, in fact, required (R. 106), and such dividends were

paid by petitioner during the taxable year (R. 86).

Petitioner apparently contends (Pet. 5) that a credit is due under Section 26 (c) (1) in any case when the contract prohibits an "asset-distribution" and that, therefore, it is entitled to the credit in the instant case since the contract, while contemplating stock dividends, prohibited payment of cash dividends. This contention is without merit.

The unambiguous terms of Section 26 (c) (1) require that before the credit becomes operative, there must be a contractual restriction against distribution of "dividends." There is no room for construing its clear provisions as applicable only to cash dividends, and, accordingly, the Commissioner, has expressly so recognized. Article 26-2 (b) (1), Regulations 94, *supra*. It is plain that Section 26 (c) (1) provides for a credit only to the extent that "dividend" payments are restricted, and not to situations where the restriction is only in respect of "asset distribution" dividends. See *Columbia River Paper Mills v. Commissioner*, 43 B. T. A. 263, 266 (on appeal to C. C. A. 9th).

The decision of the court below is not in conflict with the decision of any other circuit court of appeals, and petitioner asserts no such conflict. Nor is it in conflict with the decision of the Board

of Tax Appeals in *Paraport Theatre Leasing Corp. v. Commissioner*, 44 B. T. A. 108. In that case the Board construed the word "dividends" in Section 26 (c) (1) as meaning "taxable dividends." In the instant case, petitioner, under the contract, was not prohibited from paying dividends in preferred stock on its common stock. There is, therefore, nothing to indicate that the dividend payments permitted by the contract were not taxable dividends.¹ Cf. *Kelly Trust v. Commissioner*, 38 B. T. A. 1014, affirmed by the Eighth Circuit on July 19, 1939 (see 1939 C. C. H., Vol. 4, Par. 9624), in an opinion which was subsequently withdrawn (106 F. (2d) 1002) because of Section 214 (a) of the Revenue Act of 1939, c. 247, 53 Stat. 862, in accordance with a stipulation of the parties; *Keister v. Commissioner*, 42 B. T. A. 484 (on appeal to C. C. A. 9th); see *Koshland v. Helvering*, 298 U. S. 441; *Helvering v. Gowran*, 302 U. S. 238.

¹ Insofar as appears and insofar as we have been able to find, North Dakota law did not forbid petitioner from paying dividends in preferred stock on its common stock. And in any event, a dividend restriction deriving from statute would not seem to be the kind of restriction contemplated by Section 26 (c) (1). *Helvering v. Northwest Steel Mills*, 311 U. S. 46; *Crane-Johnson Co. v. Commissioner*, 311 U. S. 54.

CONCLUSION

The decision below is correct and there is no conflict. The petition should therefore be denied.

Respectfully submitted.

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APRIL 1942.